

CEPS COMMENTARY



Thinking ahead for Europe

Mellowing Meroni: How ESMA can help build the single market

Jacques Pelkmans and Marta Simoncini**18 February 2014**

On January 22nd, the Court of Justice of the European Union (CJEU) gave its long-awaited opinion in the case concerning the European Securities and Markets Authority (ESMA).¹ The ruling is important in order to appreciate the modern understanding of the Meroni non-delegation doctrine. It is not the purpose of this CEPS Commentary to provide a fully-fledged analysis of the ESMA ruling,² but rather to extract the potential implications of the ESMA case for the place and significance of the Meroni doctrine in building up the single market. We aim to demonstrate that the ESMA case is yet another manifestation of a slow process of “mellowing Meroni”. This is a critical condition for a new single market strategy aiming to end the remaining fragmentation of the single market – not only in financial markets but also in network industries – and ensure its ‘proper functioning’.

Debating Meroni: The ESMA case

As a derivative of the 1956 Meroni case still under the European Coal and Steel Community (ECSC),³ the non-delegation doctrine has only become a source of technical/legal debate since about the mid-1990s, and especially after lawyers began to take a more critical view of the interpretation under the Maastricht, Nice and Lisbon Treaties.⁴ A short summary of the

¹ See Case C-270/12, United Kingdom v Parliament and Council (http://curia.europa.eu/juris/document/document_print.jsf?doclang=EN&text=&pageIndex=0&part=1&mode=lst&docid=146621&occ=first&dir=&cid=82023).

² For a more comprehensive treatment, see Jacques Pelkmans and Marta Simoncini, “Putting Meroni to rest: Towards a single market for network industries”, paper presented at the European University Institute, Florence, September 2013 (under revision for forthcoming publication).

³ Cases 9/56 and 10/56, Meroni & Co, *Industrie Metallurgiche v. High Authority*, [1957-1958] ECR 133.

⁴ See A. Kreher, “Agencies in the European Community – a step towards administrative integration in Europe”, *Journal of European Public Policy*, Vol. 4, No. 2, 1997, pp. 225-245; R. Dehousse, “Misfits: EU Law and the Transformation of European Governance”, Jean Monnet Working Paper No. 2; European University Institute, Florence, 2002; D. Gerardin, R. Muñoz and N. Petit (eds), *Regulation through Agencies in the EU. A New Paradigm of European Governance*, Cheltenham: Edward Elgar, 2005; E. Chiti, “An important part of the EU’s institutional machinery: Features, problems and perspectives of

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Meroni doctrine, developed somewhat since the original 1956 case, includes the following essentials. The EU Member States have delegated powers to the EU level and one cannot presume that any such powers can, in turn, be delegated to (say) an EU agency without an explicit decision, although an explicit Treaty base is not indispensable. If powers are delegated, they cannot be 'discretionary' to such an extent that the 'wide margin of discretion' might enable the 'execution of actual economic policy'. The latter would mean an illegal transfer of responsibility (it is the delegator, not the delegate, making the policy choices) and would alter the balance of powers, later interpreted as the 'institutional balance' between the EU institutions. Any delegated powers should be embedded in or accompanied by guarantees of judicial review, transparency and active consultation. To that end, it is also required to delegate powers under precise rules and within boundaries carefully defined by the EU legislator.

The UK was seeking an annulment of Art. 28 of the ESMA regulation,⁵ which empowers ESMA to forbid short-selling in certain highly specific circumstances and under strict conditions. This competence is part of ESMA's duty to exercise proper supervision and to prevent activities that "threaten the orderly functioning and integrity of financial markets or the stability of the whole or part of the financial system in the Union" and, "if so required in the case of an emergency situation" (Art. 9(5) ESMA Regulation). The UK invoked the non-delegation doctrine that generally goes under the label of the 'Meroni doctrine' and the legal limits to harmonisation in the internal market as the grounds for seeking annulment of Art. 28. The UK employed four arguments in advocating annulment, all four of which the CJEU dismissed in their entirety.

First of all, the UK contended that in the exercise of supervisory powers on short-selling market, ESMA had been given broad discretionary tasks that may have a political nature, which would be at odds with the Meroni principle on the delegation of powers. Secondly, the UK deemed such tasks contrary to the principle set in the Romano case (C-98/80)⁶ concerning the prohibition on administrative bodies to adopt measures of general application with the force of law.

Following the Opinion of Advocate General Niilo Jääskinen, the CJEU recognised the lawfulness of the delegation of powers to ESMA as long as objective criteria and circumscribed conditions led the exercise of the delegated powers and these criteria and conditions are amenable to judicial review. According to the AG and the CJEU, the Lisbon Treaty has introduced critical guarantees that allow EU agencies to be lawfully delegated regulatory powers (such as Arts 263 and 277 TFEU on judicial review).

Nowadays, therefore, the Meroni doctrine has been updated to the changed 'constitutional' framework of the treaties. If delegation complies with the legal guarantees set by the current context of the treaties, no dangerous (and unlawful) shift of responsibility would occur.

European agencies", *Common Market Law Review*, Vol. 46, 2009; S. Griller and A. Orator, "Everything under control? The 'way forward' for European agencies in the footsteps of the Meroni doctrine", *European Law Review*, Vol. 35, No. 3, 2010; D. Sorace, "Una nuova base costituzionale europea per la pubblica amministrazione", in M.P. Chiti and A. Natalini (eds), *Lo spazio amministrativo europeo. Le pubbliche amministrazioni dopo il Trattato di Lisbona*, Bologna: Il Mulino, 2012; M. Chamon, "EU agencies between Meroni and Romano or the devil and the deep blue sea", *Common Market Law Review*, Vol 48, 2011.

⁵ Reg. 236/2012 of 14 March 2012, OJEU 2012 L 86/1.

⁶ See <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:61980CJ0098:EN:HTML>

The third plea in law of the UK concerned the infringement of Arts 290 and 291 TFEU. In the opinion of the UK, the Council could only confer to the European Commission the powers to adopt non-legislative acts of general application as well as implementing acts.

According to the Opinion of the AG, EU agencies cannot adopt the delegated acts under Art. 290 TFEU, since these are able to change the normative content of legislative acts. However, if the criteria of delegation set out in Meroni are complied with, EU agencies may be endowed with the implementing powers under Art. 291 TFEU as a “midway solution between vesting implementing authority in either the Commission or the Council, on the one hand, or leaving it the Member States, on the other” (para. 86, Opinion).

The judgment of the CJEU dismisses the plea in question, by saying that the powers conferred to ESMA do not correspond to the circumstances set in Arts 290 and 291 TFEU. ESMA’s powers in the short-selling market should be read in context with “a series of rules designed to endow the competent national authorities and ESMA with powers of intervention to cope with adverse developments which threaten financial stability within the Union and market confidence” (para. 85, of the judgment). Within the limits of the ‘updated’ Meroni doctrine, when pursuing specific policy objectives, the Council may delegate regulatory powers to EU bodies with specific technical expertise. The Court, therefore, seems to distinguish the (Meroni-compatible) delegation of powers to EU agencies that is only indirectly recognised in the Treaties, from the explicit delegation of powers to the European Commission under Arts 290 and 291 TFEU.

In its fourth plea in law, the UK alleged the infringement of Art. 114 TFEU on the harmonisation in the internal market, because its use as a legal basis for ESMA powers was *ultra vires*. The UK argued that this provision is not intended to authorise ESMA to take individual measures directed at natural and legal persons.

Relying on this plea, the AG asked the CJEU for the annulment of the provision in question, since ESMA’s special powers go beyond internal market harmonisation.

In principle and on the ground of previous case law (in particular, C-66/04, *UK v. Parliament and Council*, and C-217/04, *UK v. Parliament and Council*), the AG recognised that harmonisation measures are not to be considered to be directed only to Member States. Methods of harmonisation should be left to the discretion of the legislature, with the aim of identifying the most suitable measures, especially in complex technical domains. However, he argued that the specific hard-law, regulatory powers conferred to ESMA aimed at “intervening on the conditions of competition” (para. 45, Opinion) and as such were not covered by the treaties. To make ESMA able to legitimately exercise those powers, therefore, the AG suggested that the appropriate legal basis would be identified in Art. 352 TFEU, which usually applies when no explicit conferred power are provided in the Treaties, but nonetheless the concerned powers are necessary to achieve the goals of the Treaties.⁷

Since Art. 352 TFEU requires the unanimity of the Member States to introduce the necessary measures, the choice of this provision as the appropriate legal basis for the exercise of ESMA’s powers would have confirmed the status quo about the future integration in the internal market, here, financial markets and the stability of the financial system. The faithful follow-up of the outcome of the subsidiarity test with respect to the proper functioning of the internal financial market would still have been at the mercy of purely political interests of Member States, rather than those of the Union. If the outcome of a functional subsidiarity test, based on the harsh experience of the recent financial crisis providing compelling

⁷ Note that this article was solely referring to the internal (or common) market until Lisbon (e.g. Art. 308, EC).

empirical evidence, can be stopped by one Member State, a properly functioning single market cannot be pursued in earnest, with possibly dire consequences once again. That the CJEU established a clear link with the core idea of a functional subsidiarity test (i.e. [negative] intra-EU cross-border externalities) is clear from the following quote: "... ESMA can adopt measures under Art. 28(1) of Regulation no. 236/2012 only if, as provided in Art. 28(2), such measures address a threat to the orderly functioning and integrity of financial markets or to the stability of the whole or part of the financial system of the Union and there are cross-border implications. Moreover, all ESMA measures are subject to the condition that either no competent authority has taken measures to address the threat or one or more of those authorities have taken measures which have proven not to address the threat adequately." [para. 46, judgment]

The CJEU, however, did not support the AG on this ground. Like the AG, the Court recognised that harmonisation measures need not to be directed exclusively to Member States. What is more, the CJEU held that Art. 28 of the contested regulation aimed to improve the conditions for the establishment and functioning of the internal market in the financial field and that the conferral of powers to an EU agency was a legitimate method for pursuing such harmonisation. After first paraphrasing para. 46 again of the ruling [quoted above] the CJEU concluded: "It follows that the purpose of the powers provided for in Article 28 of Art. 28 of Regulation no. 236/2012 is in fact to improve the conditions for the establishment and functioning of the internal market in the financial field" [para. 116, judgment].

The not-so-single market for network industries and Meroni

In some (services) markets and for network infrastructures with high sunk costs, such as for energy, eCommunications and (freight) railways, the establishment and proper functioning of the single market can simply not be accomplished without selective and proportionate centralisation of some strategic tasks of rule-making and enforcement, partly indeed within EU Agencies. This is not a matter of expressing political preferences for 'more Europe' (or not), but a question of a rigorous, functional application of the subsidiarity test. In other words, if one truly pursues an integrated single market in these policy domains as well as its proper functioning, one ought to conduct a functional subsidiarity test aimed at identifying the level of government that can address the concerned task more effectively. The EU ought to act according to the outcome of the test by enacting the appropriate regulatory and/or institutional measures.

For all the enormous progress the single market has made over the last few decades⁸ in the very domains where a higher degree of centralisation via quasi-independent EU Agencies is required, the resistance is strong. There are essentially two reasons why the selective, yet indispensable centralisation is not coming about or only excruciatingly slow (and hence, is not yet effective): one boils down to vested interests of national governments or their agencies/regulators/supervisors (where relevant) and/or business segments benefitting from the fragmentation; the other one is the excuse of the Meroni doctrine. Even when the first type of resistance has become less credible or is shown to be costly for the EU or is gradually objected to by European business in light of European strategies or globalisation, the Meroni 'excuse' has been chilling or killing almost any debate about the functional need of EU Agencies. Ever since the mid-1990s, the Meroni doctrine has stalled all attempts to endow, when explicitly and carefully justified, EU Agencies with powers ensuring the proper functioning of a truly single market. The doctrine has become a convenient political

⁸ See Jacques Pelkmans, "Single market: Deepening and widening over time", *Intereconomics*, Vol. 46, No. 2, March/April 2011.

axiom amongst the EU Member States and their governments or agencies: executive functions, largely vested in the Commission, cannot be delegated to EU bodies.

The non-delegation doctrine undoubtedly has constitutional virtues and the present authors wish to emphasise those once again. Member States expect, rightly so, that the principle of conferral of powers to the EU level is not undermined. Subsequently, they expect that at the EU level a careful institutional balance is maintained between the three principal EU decision-making institutions (namely, the Council of Ministers, the European Parliament and the European Commission), in such a way that the essential (call them “political”) policy and regulatory objectives and strategies are determined and controlled by them (and nowadays, also the EP). In this general political sense, there is nothing wrong with Meroni. For the EU to be and remain a sound and legitimate Union, it is crucial that the non-delegation doctrine protects the Member States against structural shifts in essential political powers that they have not explicitly agreed to.

The problem with Meroni is not constitutional, but operational. Using Meroni as an axiom, simply because it is most convenient for national regulators/supervisors (and selectively supported by business), has proven dysfunctional for the Union and prevented the single market from coming into being in a number of sub-markets⁹ What matters for the treaty objectives, however, is that one cardinal principle – the constitutional non-delegation principle – is upheld, whilst another existential duty of the Union – the establishment and proper functioning of the single market – is vigorously pursued as well. Thus, rather than ‘manipulating’ Meroni as a freezing axiom, without serious debate and being careless about the resulting fragmentation, it is the duty of Member States and, indeed, of all three EU decision-making bodies to find a balance between these two critical drivers of the Union.

Implications of ESMA for a better functioning single market

The ESMA ruling is yet another step in a very gradual process of the EU coming to terms with the appropriate and justified degree of delegation to EU agencies (with some carefully circumscribed regulatory or intervention powers) for the completion and proper functioning of the single market. This applies to financial markets and to network industries, mostly with large sunk costs. One can observe a highly cautious beginning in e.g. the functioning of EASA (for technical inspections and certification of aircraft), the proposed expansion of ERA (for rail) powers to EU-wide licensing of rolling stock, the consecutive shifts of supervisory powers via a new banking supervisory agency (EBA) to the ECB (a genuine and fully independent EU agency under the treaty) and this time with (bank) resolution powers, and the political battles about the gas/electricity agency (ACER) and the one for eCommunications (BEREC, in fact, more like a common subsidiary of the national agencies).

The ESMA ruling shows clearly that, with the important proviso of convincing conditions and appropriate guarantees of legitimacy, transparency and judicial review, the single market could benefit from EU agencies fulfilling similar functions in such sub-markets as (quasi-independent) technical agencies all over the world – and indeed in national markets

⁹ How deeply fragmented the internal market for network industries (with infrastructures with large sunk costs) still is after some 25 years of EU liberalisation and EU regulation, is perhaps too little realised. A wake-up call is provided in Jacques Pelkmans and Andrea Renda, “Single eComms market? ...no such thing”, *Communications & Strategy*, No. 82, Spring, 2011. The deep fragmentation is confirmed for eComms, freight rail and gas/electricity in European Commission, “Market functioning in Network Industries”, DG EcFin European Economy Occasional Paper No. 129, February 2013. Many other sources are referred to in Pelkmans & Simoncini, op. cit.

in the EU – routinely do – namely by ensuring that such markets function properly by detailing the regulatory regimes and intervening, if necessary, immediately to prevent harm.

What would be most undesirable is to toss away the Meroni doctrine. Rather, what is urgently needed is to ‘mellow’ the application of the doctrine, but only in those instances where a compelling case has been made for the sake of the establishment and proper functioning of the single market, the core economic function of the Union.

In light of the Lisbon institutional framework as set in the Treaties and the CJEU case law, the ESMA judgment of the CJEU seems to confirm the acceptability of a ‘mellow’ interpretation. In fact, ‘mellowing Meroni’ is not about rejecting the constitutional principle of legitimate delegation itself, but it is rather about finding a balance between this fundamental principle and the principle of establishing and ensuring the functioning of the internal market surrounded by legal conditions and guarantees. Exactly as the CJEU has confirmed in the ESMA case, Meroni is not there to freeze half-baked integration, if not sometimes fragmentation, of the internal market.